Supreme Court, U.S.
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No. 93 -

In The
Supreme Court of the United States
October Term, 1993

JOHN E. FILIOS, ET AL.

PETITIONERS

v.

COMMISSIONER OF REVENUE OF MASSACHUSETTS

RESPONDENT

PETITION FOR WRIT OF CERTIORARI TO THE SUPREME JUDICIAL COURT FOR THE COMMONWEALTH OF MASSACHUSETTS

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QUESTION PRESENTED

Does the Commonwealth of Massachusetts's policy of requiring federal military retirees to pay state income tax on their military retirement benefits while it completely exempts from state tax the retirement benefits of state and municipal retirees violate 4 U.S.C. §111 which prohibits states from taxing federal employees in a discriminatory fashion?

LIST OF PARTIES

The parties to the proceeding below were the petitioners, who are federal military retirees and their spouses: John E. Filios, Eleanor G. Filios, Herbert L. Cheeseman, Betty B. Cheeseman, Ralph Cipolla, Doris H. Cipolla, Joseph M. Conroy, Robert C. Davenport, Annetta B. Davenport, Kenneth R. Depperman, Mary E. Depperman, Charles F. DeSmet, Marjorie I. DeSmet, Francis H. Fumia, Dreama F. Fumia, Mack K. Greenberg, Harriet C. Greenberg, Daniel F. Hayes, Dorothy R. Hayes, David J. Mainville, Vern Mainville, Donald G. Smith, Ruth E. Smith, Richard J. Spatafora, Liliane M.J. Spatafora, Russell E. Tracy, and Lillian A. Tracy. The respondent before the Court is the Commissioner of Revenue of the Commonwealth of Massachusetts.

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TO THE HONORABLE, THE CHIEF JUSTICE AND ASSOCIATE JUSTICES OF THE SUPREME COURT OF THE UNITED STATES

Petitioners John E. Filios et al. respectfully pray that a writ of certiorari issue to review the judgment and opinion of the Supreme Judicial Court for the Commonwealth of Massachusetts, entered in the above-titled case on July 13, 1993, as amended by that Court on October 26, 1993.

OPINION BELOW

The opinion of the Supreme Judicial Court is reported at 415 Mass. 806 (1993) and is reprinted in the Appendix hereto, p. A. 44-51, infra. The decision of the Court was amended by the Court on October 26, 1993. A. 52.

JURISDICTION

The jurisdiction of this Court to review the judgment of the Supreme Judicial Court is invoked pursuant to 28 U.S.C. § 1257.

STATUTE INVOLVED

This case involves 4 U.S.C. § 111 which provides, in material part, as follows:

> The United States consents to the taxation of pay or compensation for personal service as an officer or employee of the United States, . . . by a duly constituted taxing authority having jurisdiction, if the taxation does not discriminate against the officer or employee because of the source of the pay or compensation.

STATEMENT OF THE CASE

Preliminary Statement

This case involves fourteen veterans[1] who have been required to pay state income tax on their military retirement benefits. It raises one issue: is it lawful under federal law for the Commonwealth of Massachusetts to compel retired military personnel to pay a state income tax on their retirement benefits when the state permits retired state and municipal workers to escape paying any such tax on their benefits?

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1. Originally 14 veterans' cases (involving a total of 27 taxpayers) were consolidated and decided by the Massachusetts Appellate Tax Board. A. 7-8. The veterans filed a single appeal. A. 45, n. 2. The Supreme Judicial Court determined as a matter of state procedure that 13 appeals were not properly before it. Id. However, on October 26, 1993, that court reconsidered and amended its judgment in order to allow all 27 taxpayers to seek review in this Court. A. 52. The same issue is raised in all 14 cases.

Federal law, codified in 4 U.S.C. § 111 and derived from the constitutional principle of intergovernmental tax immunity, prohibits states from tax discrimination against federal employees. Since retirement benefits for both federal veterans and state and local employees are derived from funds never subject to federal income tax, the two systems are essentially identical. Thus, Massachusetts' favoritism to its own retirees is illegal.

Several recent decisions of this Court have relied on section 111 to strike down state efforts to tax federal employees while protecting their own workers. Massachusetts' actions here not only flout the clear tenor of those decisions but also, if allowed to stand, open a door which other states can use to bypass the equal treatment command of section 111.

Statement of Facts and Prior Proceedings

The facts in this case are simple and undisputed.[2] The 14 veterans who ask this Court to hear their case are residents of the Commonwealth who received income from military retirement benefits between 1985 to 1988 ("the veterans"). A. 3. They paid Massachusetts income tax on that income and filed timely abatement applications with the Commissioner of Revenue ("Commissioner") which were denied. A. 45. They appealed to the Appellate Tax Board ("Board"). Id.

On October 8, 1991, the Board ruled in the Commissioner's favor. A. 1. The veterans sought reconsideration in light of the intervening decision in Barker v. Kansas, __ U.S. __, 118 L. Ed. 2d 243 (1992). On July 1, 1992, the Board denied reconsideration and issued its Findings of Fact and Report. A. 2-43.

The veterans filed a timely appeal to the Massachusetts

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2. The discussion of facts in this petition will be based on the Appellate Tax Board's decision below, A. 2-43, and on the Supreme Judicial Court's opinion. A. 44-51.

Appeals Court pursuant to Mass. G.L. c. 58A, §13. A. 45. On October 2, 1992, the Supreme Judicial Court allowed the veterans' application for Direct Appellate Review. Id. That court issued a decision against the veterans on July 13, 1993. A. 44-51. On October 26, the Court amended its judgment to reflect that all 14 veterans, and the 13 spouses were properly parties to the appeal. A. 52; see A. 45, n.2.

SUMMARY OF ARGUMENT

In the past four years this Court has held that federal law, derived from basic constitutional principles of federalism, bars states from using their tax systems to favor their employees or retirees over federal workers or retirees. Yet the Supreme Judicial Court of Massachusetts has upheld a policy which requires retired military personnel to pay state income tax on their retirement benefits while exempting all of its own state and local retirees from that tax. If that policy is allowed to stand, Massachusetts will have shown other states a clear path to circumvent this Court's decisions and federal law.

As discussed below, three separate lines of argument show that Massachusetts is illegally taxing retired federal military personnel. First, as the Supreme Judicial Court recognized, state laws still exist which expressly exempt state and local retirees, and only them, from tax on their pensions. This facial statutory discrimination violates federal law. Massachusetts' defense, that petitioners did not show how many state and local retirees are benefitting from this discrimination, not only seeks to shift the state's burden onto petitioners, but it directly conflicts with this Court's precedents in other areas where it has considered claims of illegal state tax favoritism.

Second, the state's primary argument, that the state and federal military retirement systems are distinguishable because the first is "contributory" while the second is not, fails because under Massachusetts' own laws 90% of state retirement benefits are paid from "pension" funds which are expressly not "contributory." The

state court allowed Massachusetts to shield a totally non-contributory pension system behind the veil, and a thin one at that, of a contributory annuity system. Unless checked by this Court, this ruse can and will be adopted by other states which seek to provide favored tax treatment to their employees.

Finally, even accepting Massachusetts' effort to fuse its pension and annuity benefits into one system, that system is not sufficiently "different" to warrant exempting its benefits from all taxation while still taxing federal military pensions. The state's self-serving decision to let its employees avoid paying federal income tax on their "contributions" converts the state system into one which, whatever it may be called, is effectively indistinguishable from the military system. Exempting state benefits while taxing federal benefits is therefore illegal discrimination.

REASONS FOR GRANTING THE WRIT

I. 4 U.S.C. § 111 PROHIBITS TAXING MILITARY RETIREES' RETIREMENT BENEFITS WHEN STATE AND MUNICIPAL RETIREMENT BENEFITS ARE NOT TAXED.

A. Davis, Barker, and the Requirement that the State Must Demonstrate Significant Differences.

This case involves the legality of Massachusetts' policy of taxing the retirement benefits of retired federal military personnel while exempting from tax retirement benefits received by retired state and municipal employees. The key question is whether this discrimination violates the terms established by Congress when it decided to give the states any authority to tax federal employees.

The Congressional decision to partially cede the federal government's sovereign constitutional immunity from state taxation of its employees, see, e.g. M'Culloch v. Maryland, 4 Wheat. (17 U.S.) 316 (1819), was made on the condition that such taxation had

to be equitable, that is, states could not tax federal employees more onerously than they taxed their own employees. See Davis v. Michigan Dept. of Treasury, 489 U.S. 803 (1989). This rule is set out in 4 U.S.C. § 111 which provides that the United States consents to taxation of its officers' and employees' pay and compensation ". . . if the taxation does not discriminate against the officer or employee because of the source of the pay or compensation."

This principle has been developed in two recent cases in which this Court struck down state efforts to discriminate in favor their retirees. See Davis v. Michigan, 489 U.S. 803 (1989); Barker v. Kansas, 503 U.S. ___, 118 L.Ed.2d 243 (1992). In Davis the Court held that the non-discrimination clause of section 111 applies to retirement benefits paid to retired federal employees and that individual retirees could sue to obtain the protection of that clause. 489 U.S. supra at 808-810, 814-15. The Court rejected Michigan's argument that the allegedly more generous benefits federal retirees receive was a "significant difference" that justified discrimination between state and federal employees. It found that the state's argument that federal employees receive more generous retirement benefits than state employees, even if true, did not warrant a "blanket exemption" for state retirement benefits which favored state employees over federal workers. Id. at 817. As Justice Kennedy wrote:

> The danger that a State is engaging in impermissible discrimination against the Federal Government is greatest when the State acts to benefit itself and those in privity with it. . . . Taxes enacted to reduce the State's employment costs at the expense of the federal treasury are the type of discriminatory legislation that the doctrine of intergovernmental tax immunity is intended to bar.

489 U.S. at 815, n.4

In Barker, the Court restated its Davis holding that, in

applying the nondiscrimination clause of section 111, the appropriate inquiry is "whether the inconsistent tax treatment is directly related to, and justified by, significant differences between the two classes." 118 L. Ed. 2d at 249 (citation omitted)(emphasis supplied). The Court concluded that military retirees are entitled to the protection of section 111 and reversed a decision by the Kansas Supreme Court that there were significant differences between federal military and state civilian retirees. Id. at 254.[3]

Both Davis and Barker focus solely on differences in the way the state treats federal and state retirees. "As the law stands, a tax that favors state and local retirees over federal retirees violates [inter]governmental immunity even if the latter are treated no differently than private retirees." A. 32 (Appellate Tax Board). As shown below Massachusetts' tax laws, both facially and as applied, favor state and municipal retirees and that favoritism is not justified by any "significant difference" between the two groups.

B. The Statutory Tax Exemption for State But Not Federal Retirement Benefits Violates 4 U.S.C. §111.

The bulk of the decision below rests upon the conclusion that the relevant distinction in Massachusetts law is not between federal and state employees but between "contributory" and "non-contributory" pension systems. A. 47. But the validity of that distinction need not be addressed, because Massachusetts' law still reflects a long-standing, explicit state policy of absolutely exempting certain state and local pensions from tax.

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3. In Barker the Court noted that while the Kansas Supreme Court had observed that state retirees contribute to their retirement funds while military retirees do not, it did not base its holding of a "significant difference" on that point. Id. at 254, n. 5. The contributory/non-contributory issue thus was not decided in Barker.

From the enactment of the first Massachusetts income tax in 1917, the state exempted pensions received by Boston school teachers and municipal police and fire personnel. A. 49, citing Sp. St. 1917, c. 327; St. 1917, c. 270. In 1973 the state Legislature provided that "[n]otwithstanding any general or special law to the contrary, income from a noncontributory annuity or pension allowance . . . shall be exempt from taxation under [the income tax.]" A. 49, citing St. 1973, c. 876, §1. This law continues in effect. A. 35.[4] These exemptions, reinforced by the Legislature in 1973, demonstrate that, on its face, Massachusetts law favors some public retirees over federal retirees, exactly the situation prohibited by federal law. See Davis, 489 U.S. supra at 815, n.4.

The Supreme Judicial Court's response to this showing of favoritism was to change the relevant test and shift the burden from the state to the veterans.[5] It accepted the Board's ruling that the state's laws "taken together do not deny to federal employees generally any favorable treatment they give to state and local government employees." A. 14 (emphasis added) Neither the court nor the Board cited any authority for adding a "generally" gloss to Barker and Davis.

The court adopted the Board's criticism of the veterans for

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4. The Board found that between 1934 and 1945 the state gradually required public retirement systems to become "contributory." A. 35. But the statutes the Board cited mandated only that newly hired employees must contribute to retirement funds; current employees could stay in pre-existing non-contributory systems. A. 34-35. Thus, as the Board recognized, some public employees remained in non-contributory plans well after 1945. Id.

5. The lower court's entire discussion of this point consists of a long quote from the Appellate Tax Board's decision and so the court must be considered to have adopted the Board's rationale. A. 49-50.

not presenting evidence as to which and how many state or local employees still benefit from these exemptions. A. 49, quoting A. 14-15, 34-35. The court held it was the veterans' "responsibility" to introduce evidence on this point and that without such evidence it could not find there were any such employees. Quoting the Board, the court opined "it is unlikely [such employees] were numerous, or that they will survive long enough to require legislative action to remove their more favorable treatment." A. 49-50. The Board could not find that there "is now an active and significant class of state or municipal employees receiving non-contributory retirement benefits" which are exempt from Massachusetts tax. A. 15.[6] It added

> "survival of any persons entitled to the exemptions granted in 1917 hardly justifies a finding of current legislative discrimination in favor of local retirees. The appellants made no attempt to prove that any actual discrimination occurred against military retirees as a result of the 1917 exemptions."

A. 35.[7]

None of this bears any relationship to Barker or Davis. Neither case required federal retirees to show an "active and significant class" favored by the state or that "actual discrimination"

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6. The court showed rather little imagination. An employee who joined a non-contributory retirement system in 1937 at the age of 21 would be only 76 today, not necessarily older than a federal military retiree who, unlike him, must pay state income tax on his non-contributory retirement benefits.

7. The court and Board faulted the veterans for not to rebutting a defense the state never raised; that these exemptions have lapsed into desuetude. Surely the veterans are entitled to rely on the legal effect of unrepealed state laws unless and until the state itself demonstrates they have lapsed and should be ignored.

was being practiced. Plaintiffs showed facial statutory discrimination in favor of state retirees. That showing having been made here,[8] the veterans are entitled to prevail.

This Court's decisions hold that the basic rule of intergovernmental tax immunity is simple. A state taxing scheme discriminates against those associated with the federal government if "it treats someone else better than it treats them." Washington v. United States, 460 U.S. 536, 545 (1983) (emphasis added).

There is no quantitative threshold of discriminatory impact below which a state can shelter a violation of intergovernmental tax immunity. Application of that principle "does not depend upon the amount of the exaction, the weight of the burden or the extent of the resulting interference with sovereign independence. Where it applies, the principle is an absolute one wholly unaffected by matters or distinctions of degree." TrinityFarm Construction Co. v. Grosjean, 291 U.S. 466, 471 (1933).[9]

Even though only a limited number of retirees may still benefit from Massachusetts' statutory favoritism, the resulting

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8. Massachusetts' statutory favoritism to state and municipal retirement benefits extends beyond the laws just discussed. For example, under Mass. G.L. c. 32, §19, the rights of a member of a Massachusetts state or local retirement system to an annuity, pension or retirement allowance are totally exempt from taxation, including the state income tax. A. 18. Federal retirement benefits enjoy no such privilege.

9. In Schuykill Trust Co. v. Pennsylvania, 296 U.S. 113, 120 (1935) the Court held that a Pennsylvania tax scheme was invalid because the burden of the tax was "lifted in respect of some securities." (Emphasis added). See also Phillips Chemical Co. v. Dumas Indep. Sch. District, 361 U.S. 376, 381 n.6 (1960) ("[a]lthough the exceptions . . . reduce the extent of the discrimination . . . they obviously do not eliminate it.").

discrimination is unambiguous. In enacting 4 U.S.C. § 111, Congress granted states the privilege to tax federal employees but only on a strict condition of non-discrimination. Since Massachusetts' highest court has conceded the state does not meet that condition, it cannot utilize the privilege granted by section 111.

C. Exempting State and Municipal Non-Contributory "Pension" Benefits From Taxation Is Prohibited By 4 U.S.C. §111.

Having chosen to discount the state laws which expressly exempt some non-contributory public pensions from taxation, the court below focussed exclusively on Mass. G.L c. 62, §2(a)(2)(E) which exempts from state tax benefits from "contributory" pension systems of state, local and federal employees. A. 47. It held that the pension systems of Massachusetts state and local retirees are "contributory" while the federal military pension system is "non-contributory." That distinction, it concluded, is a "significant difference" sufficient to pass muster under section 111. Id.

The first flaw in this reasoning is that the Massachusetts public retirement program is not the simple one-dimensional system the court's opinion suggests. By law Massachusetts defines each employee's retirement benefit as having two components, an "annuity" derived from employee contributions and a "pension" which comes exclusively from "contributions made by the appropriate governmental unit." See Mass. G.L. c. 32, §1, ¶¶ 8,30. Yet the state exempts from tax the entirety of state and local retirement benefits, not just the contributory "annuity" portion.

Thus, whatever section 2(a)(2)(E) seems to say, in practice, Massachusetts exempts non-contributory "pensions" which its retirees receive. Since those benefits are derived solely from employer-supplied funds, the contributory/non-contributory dichotomy, the sole basis upon which the Supreme Judicial Court upheld discrimination against the veterans, is irrelevant.

State and municipal retirees receive non-contributory

"pensions" and pay no taxes on them. Indeed that non-contributory "pension" comprises approximately 90% of state employees' retirement benefits. A. 49.[10] Because that retirement benefit is "non-contributory," there is no "significant difference" between it and the retirement benefits received by the veterans here.

The state cannot defend exempting these non-contributory "pensions" from tax on the ground that its retirees also receive contributory "annuity" benefits. First, as noted in Davis, that argument would only justify exempting the contributory portion of benefits state retirees receive, not the "blanket" exemption the state has actually given. Davis, 489 U.S. supra at 817.

Second, a system of derivatory exemptions would itself be discriminatory, and so violate section 111 because federal military retirees do not have a comparable opportunity to shelter their non-contributory retirement benefits from state tax by mixing them with contributory pension benefits at a ratio of nine parts to one.

Massachusetts' policy of exempting non-contributory "pension" benefits paid to state retirees while taxing veterans' non-contributory retirement benefits discriminates against federal employees. This violates the plain language of 4 U.S.C. § 111. Davis v. Michigan, supra. Since the state has not demonstrated a "significant difference" between those two types of benefits, it is not longer entitled to exercise the Congressionally granted privilege of taxing petitioners' retirement benefits.

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10. Contrary to the implication below, A. 48-49, petitioners' argument is not that state employees contribute so little as to make the entire state retirement system "non-contributory." Rather they argue that one of the two separate retirement systems the state effectively operates, the "pension" system, is unambiguously non-contributory in any sense of the word. Thus there is no basis upon which the state can justify not taxing those non-contributory benefits while still taxing federal military retirement benefits.

D. Massachusetts' Retirement System is Effectively Identical to the Federal Military System, so Exempting State Benefits Violates 4 U.S.C. §111.

A second flaw in Massachusetts' effort to shelter its exemption of public retirement benefits under the "contributory" umbrella is that the state's retirement system is not, under its own definition, really "contributory" at all.

Massachusetts has a unique form of "contributory" retirement system. In 1987, the state amended Mass. G.L. c. 32, §22(10), so its employees no longer make any contributions, as that term is normally understood, to their retirement systems. See St. 1987, c. 697, §75. As amended, section 22(10) provides in part:

> Each government unit . . . shall assume and pay the contributions which would be payable by the employees as members . . . . Such contributions, although designated as employee contributions, will be paid by the applicable governmental unit . . . in lieu of contributions by the employee . . . . The contributions so assumed shall be treated as employer contributions in determining tax treatment under the United States Internal Revenue Code. The contributions so assumed shall be treated and identified . . . as member contributions for purposes of the retirement system . . . and for all purposes of chapter sixty-two [the state income tax].

While state employees do pay state tax on their "contributions," they no longer pay federal income tax on them. A. 19; 26 U.S.C. §414(h)(2).[11] Thus the lower court's statement, A.

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11. Because Massachusetts uses the federal definition of "gross income" to define income for state tax purposes under Mass. G.L. c. 62, §2(a), state employees should also escape paying any state income tax on their retirement "contributions." But when its own revenues are involved, the state is less willing to accept its

48, that "employees already have been taxed on the contributions they make to their pensions," is misleading. There is little economic difference between a soldier earning $30,000 per year with the United States contributing $2000 to his retirement fund and a state employee who "earns" $32,000 per year with $2000 taken off the top as a pre-tax pension "contribution." Giving "contributory" its ordinary, common sense meaning, Massachusetts has not had a "contributory" retirement system since 1987.

Massachusetts shares this common sense understanding of what a "contributory" retirement system is. In his published response to Barker, which the Supreme Judicial Court cited twice, the Commissioner stated that employee "contributions" can only come from funds previously subject to taxation.

> "A contributory pension is one in which amounts contributed to the plan are includible in the Massachusetts gross income of the employee . . . . Under a non-contributory plan, amounts contributed on behalf of an employee are not included in the gross income of the employee and are therefore not subject to tax at the time of contribution."

Technical Information Release ("TIR") 92-3, A. 47, n. 4; A. 48.[12]

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legal fictions. The state requires taxpayers to add back into adjusted state income "contributions" excluded from federal gross income. Mass G.L. c. 62, §2(a)(1)(I).

12. By inserting "Massachusetts" before "gross income" the Commissioner avoided explicitly defining the state's system as "non-contributory." But neither he nor the lower court made any effort to explain why re-inclusion of "contributions" into state adjusted gross income should have a greater consequence than their exclusion from the federal gross income.

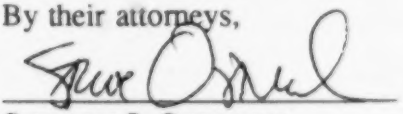
Since 1987, state "employee contributions" have not been included in employees' federal gross income. Using the Commissioner's own logic, the state's system thus is effectively non-contributory. Once again, the sole basis the state has relied upon to distinguish between federal and state retirees has vanished and the Court confronts a plainly unlawful effort to tax federal retirees while exempting state retirees.

Plainly Massachusetts wishes to have its cake and eat it too. It classifies contributions to state and local retirement funds as employer contributions when that works to employees' advantage and classifies them as employee contributions when that, diametrically opposite, conclusion works to their advantage. This distortion of the state's tax laws in order to "benefit itself and those in privity with it" is just the sort of scheme to reduce state employment costs which Justice Kennedy held is barred by section 111. Davis, 489 U.S. supra at 815, n.4.

CONCLUSION

For the foregoing reasons, petitioners request that their application for a writ of certiorari be granted.

Respectfully submitted,
John E. Filios et al.
By their attorneys,



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DATED: Boston, Massachusetts: November 16, 1993.

The Commonwealth of Massachusetts
Appellate Tax Board

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Docket No(s). 171106, 170813-170814,
171107, 171216, 171711,
171828, 171831, 172022

JOEN E. & ELEANOR G. FILIOS, et al,

Appellants

COMMISSIONER OF REVENUE,

Appellee

DECISION

Decisions for the Appellee. Appellants' Consolidated Request for Conclusions of Law, Nos. 1 through 6, are refused. Chairman Timothy P. O'Brien did not participate in the consideration or decision of these appeals.

APPELLATE TAX BOARD

By _____ Chairman

_____ Member

_____ Member

_____ Member

_____ Member

Attest: _____ Clerk

Date: October 8, 1991

(Seal)

Income tax

NOTICE: An appeal may be taken to the Appeals Court by either party to these proceedings. A claim of appeal should be filed with this Board in accordance with the Massachusetts Rules of Appellate Procedure.

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COMMONWEALTH OF MASSACHUSETTS

APPELLATE TAX BOARD

JOHN E. and ELEANOR G. FILIOS,

et al.

v. COMMISSIONER OF REVENUE

Docket Nos. 171106, 170818-170824, 171107, 171216

171711, 171828, 171831, 172022

Promulgated: July 1, 1992

This is an appeal under the formal procedure pursuant to G.L. c.62C s.39, as amended, from the refusal of the appellee to abate income taxes assessed under G.L. c.62 s.2 for the tax years 1985 through 1988.

These findings of fact and report are made pursuant to a request by the appellants under G.L. c.58A s.13, as amended,

and Rule 32 of the Rules of Practice and Procedure of the Appellate Tax Board.

Robert E. Dickinson, Esq., for the appellant.

Constance M. Simon, Esq., for the appellee.

FINDINGS OF FACT AND REPORT

The appellants are residents of the Commonwealth who received income from military retirement compensation from the United States, based on the details of their military service, during some or all of the tax years at issue. This compensation was included in the federal gross income of each appellant, and thus became part of each appellant's Massachusetts gross income. Each appellant paid the taxes due on the retirement compensation. The military retirement system is a non-contributory system: military personnel do not have a separate, identified amount deducted periodically from their pay and deposited in a segregated retirement fund from which retirement benefits are paid. (It appears that since 1984, under

P.L. 98-94, s.925, funds appropriated annually and charged to the manpower budget of the Department of Defense are transferred to a Military Retirement Fund administered by the Treasury Department.) The board's findings are based in large part on a Stipulation of Agreed Facts submitted by the parties and on the exhibits attached thereto.

The appellants are members of various military organizations which in turn are members of an umbrella organization, the Massachusetts Council of Military Organizations (MASSCOMO), whose counsel represents all of the appellants. On or about March 3, 1988, MASSCOMO requested a ruling from the Department of Revenue that military retirement pay was not taxable. Stipulation, Exhibit 3. In a letter dated February 16, 1989, the Commissioner replied that military retirement pay was taxable. Stipulation, Exhibit 4.

On March 28, 1989 the United States Supreme Court issued its decision in the case of Davis V. Michigan Department of the Treasury, 489 U.S. 803 (1989), holding that the Michigan

income tax violated the federal intergovernmental immunity statute by denying to retired federal civil service employees the favorable treatment accorded to retired state and local governnent employees. Stipulation, Exhibit 5. On May 10, 1989, the Commissioner of Revenue issued a Technical Information Release (TIR 89-6) stating that the Davis decision did not affect the Massachusetts tax treatment of federal retirement income, including military retirement income. Stipulation, Exhibit 6. By letter dated November 14, 1989, the Rulings and Regulations Bureau denied MASSCOMO's request to reconsider the Commissioner's position. Stipulation, Exhibits 7 and 8.

In the meantime the appellants had filed applications for abatement or amended returns excluding their military retirement income for some or all of the tax years 1985-1988, the appellee had denied the applications and some of the appellants had already filed their appeals with the Appellate Tax Board. The table below summarizes the data affecting the

board's jurisdiction in these appeals. The board found that the requirements of its jurisdiction had been met in Docket numbers 170818, 170819, 171107 (1985 only), 170821 (1985, 1988), 171106, 171828 (1987, 1988), 171831, 171711 (1987), and 170824 (1986, 1987). In each of the remaining appeals listed the fulfilment of one or more of the conditions of jurisdiction is at least doubtful. In view of the board's decision for the appellee on the merits of all of the appeals, however, a finding of jurisdiction would not affect the result of any of them.

Table of Jurisdictional Facts

Taxpayer	Docket No.	Fiscal year	Return filed	Application Filed	Application Denied	Appeal filed
Cheeseman	170818	1985	3/25/86	4/14/89	9/12/89	10/30/89
		1986	4/7/87			
		1987	3/29/87			
Cipolla	170829	1985	4/12/86	4/18/89*	10/4/89	10/30/89
Conroy	170819	1985	3/21/86	3/31/89	10/3/89	10/30/89
Davenport	171107	1985	4/14/86	4/17/89	9/22/89	11/17/89
		1986	*	*		
		1987	10/17/88*			
Depperman	171216	1986	*	5/31/89	11/10/89	11/29/89
		1987	*	*		
		1988	*	*		
DeSmet	170821	1985	4/15/86	5/3/89	11/10/89	1/5/90
		1986	*	*		
		1987	2/5/88*			
		1988	2/2/89			
Filios	171106	1986	4/11/86	4/15/89	9/22/89	11/17/89
Fumia	171828	1986	*	7/4/89	11/10/89	1/5/90
		1987	2/20/88			
		1988	4/17/89			
Greenberg	171831	1985	4/10/86	7/1/89	11/10/89	1/5/90
		1986	4/10/87			
		1987	4/10/88			
Hayes	171822	1985	7/21/86#	6/5/89	9/14/89	1/30/89*
		1987		4/1/88#		
Mainville	171711	1986	*	9/25/89	12/20/89	12/26/89
		1987	4/12/89		9/18/89	
		1988	*		9/18/89	

(continued on next page)

Table of Jurisdictional Facts (continued)

Taxpayer	Docket No.	Fiscal year	Return filed	Application Filed	Application Denied	Appeal filed
Smith	170823	1985	2/18/86#	4/14/89	10/4/89	10/30/89
Spatafora	172022	1987	*	10/6/89	5/8/90	
		1988	*	10/12/89	12/10/89	1/22/90
Tracy	170824	1986	1/28/87	6/1/89	9/14/89	10/30/89
			1987	2/1/88		10/30/89
			1988	*		

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* Data missing or questionable
\# Check or bill date from DOR printout

Source: Appellants' Exhibit: Jurisdictional Documents

Income from a contributory retirement fund of the United States government, the commonwealth, or any political subdivision thereof, to which the employee has contributed, is deductible from Massachusetts gross income. Although the military retirement system is not contributory and the appellants have not contributed to it, the appellants contend that they had made "imputed contributions" toward their retirement benefits through reduced salaries, and therefore are entitled under the Davis case to be treated in the same manner as Massachusetts public employees, whose contributory retirement pay is exempt. In support of this position they placed in evidence several congressional documents.

A Study of the Military Retired Pay System and Certain Related Subjects is a Report to the Committee on Armed Services of the United States Senate by the Study Committee of the University of Michigan, dated July 6, 1961 (87th Congress, 1st Session), submitted as appellants' Exhibit 1. One of of the matters that the Committee asked the study to

address was the possibility of adopting a contributory retirement system. Exhibit 1 p. 1. The report states, "Retired pay is, in a real sense, a system of deferred pay designed to assist officers and enlisted men make the transition to civilian life and to provide basic economic security in the event that such a transition cannot readily be made." Exhibit 1 p. 8. Chapter VIII, "Contributory Vs. Non-Contributory Retirement Plans," states that although contributory plans predominated in private industry, many of the larger plans were non-contributory, probably non-contributory plans covered more employees, and during the past decade there had been a substantial trend toward non-contributory plans. The report states that the military retirement plan in the United States had always been non-contributory and without advance funding. Exhibit 1 p. 65. The report says that the establishment of a contributory system would not produce significant savings to the government and on the contrary would probably require increases in pay to offset the effect of the contribution on military employees, in addition

to administrative costs of maintaining an account for each employee. Exhibit 1 pp. 66-67. The report concludes that Congress should not adopt a contributory system. Exhibit 1 p. 68.

Report No. 549 from the Committee on Armed Services titled Uniformed Services Pay Act of 1965 (appellants' Exhibit 2), prepared to accompany H.R. 9075, states that the military pay increase proposed therein "fully recognizes the tax advantage and the non-contributory retirement aspect of military compensation and takes them into account." Exhibit 2 p. 18; see also pp. 20-26. The act itself, P. L. 89-132, dated August 21, 1965, was in evidence as appellants' Exhibit 3.

Report No. 92-82, Amending the Military Selective Service Act of 1967; to Increase Military Pay; to Authorize Military Active Duty Strengths for Fiscal Year 1972; and for Other Purposes, a report dated March 25, 1971, from the House Committee on

Armed Services to accompany H.R. 6531, was in evidence as appellants' Exhibit 4. It proposes increases in regular military compensation to levels bearing a reasonable relationship to civilian wages for similar work and recognizes that regular military compensation does not include a specific retirement contribution. Exhibit 4 p. 24. The act itself, P.L. 92-129, September 28, 1971, was in evidence as appellants' Exhibit 5.

Although these documents provide evidence that military pay was lower than it would have been had the retirement system been financed by employee contributions, in the board's opinion they fall short of demonstrating an "imputed contribution."

The appellants' next contention is that in taxing their military retirement compensation, the Massachusetts income tax discriminates against them, in violation of the constitutional principle of intergovernmental immunity as embodied in 4 USC s.111, and in violation of the income-tax authorization contained in Article 44 of the Amendments to the Massachusetts

Constitution, because the non-contributory retirement compensation of certain public employees of Massachusetts cities and towns are specifically exempted from tax.

Exemptions from income tax were made in 1917 for pensions and annuities paid from funds established for the purpose for annuities paid by cities and towns on account of service in a police or fire department (St. 1917 c.270) and for public school teachers in Boston (Sp. St. 1917 c.327 s.1). In 1936 all city and town retirement plans were made contributory; but some employees did not elect to join the contributory system, and in 1973 income from non-contributory annuities and pensions received for service in the police or fire department of a city or town by a person who was employed when the contributory system was established and did not elect to join the contributory system was expressly exempted from income tax (St. 1973 c.876 s.1). In an "information letter" dated June 11, 1990, counsel to the appellee's Rulings and Regulations Bureau told one of the appellants that to the best of

his knowledge St. 1973 c.876 had been neither repealed nor amended. Appellants', Exhibit 11.

Unlike the Michigan statute at issue in Davis, the Massachusetts statutes taken together do not deny to federal employees generally any favorable treatment that they give to state and local government employees. Income from contributory plans of the federal government is exempt from Massachusetts income tax in the same manner as income from contributory plans of Massachusetts state and local governments. The only exemptions provided for non-contributory retirement benefits are given for service in a local police or fire department and for Boston public school teachers. Both of these exemptions were enacted in 1917, the year after the imposition of the income tax. In order to be covered by a non-contributory plan whose exemption was confirmed by St. 1973 c.876 s.1, an employee in the police or fire service of a city or town would have to have been in active service when the contributory system under Chapter 32 was

established in 1936 or 1937 and elected not to join it. If any qualifying employees existed during the tax years at issue, it was the responsibility of the appellants to produce evidence of the fact. Since no such evidence was furnished to the board, no finding can be made that the classification established by St. 1917 c.270 and confirmed by St. 1973 c.876 had any members during the years at issue. Further, the board notes that the active life of a person in the police or fire service would be unlikely to have continued for 55 years from 1936, when the municipal retirement plans were made contributory, to 1991. If the class had any members during the years at issue, it is unlikely that they were numerous, or that they will survive long enough to require legislative action to remove their more favorable treatment or give similar treatment to military retirees. The board therefore did not find that there is now an active or significant class of state or municipal employees receiving non-contributory retirement benefits which are deducted in determining Massachusetts gross income under the provisions of

G.L. c.62 s.2(a)(2)(E), or that under the standard of Davis the Massachusetts income tax discriminates against federal military employees.

The board therefore decided for the appellee in all of the appeals for all of the fiscal years at issue.

OPINION

Private or governmental pensions, including military retirement benefits, are included in gross income for purposes of the federal income tax. IRC s.61(a)(11); Reg. s.1.61-11. Massachusetts gross income is federal gross income with certain additions and deductions. G.L. c.62 s.2(a).

The appellants cite several cases for the proposition that a pension is not income for Massachusetts income tax purposes: Lyon v. Commissioner of Corp. & Tax., 258 Mass. 450 (1927), holding that a retirement allowance paid to a professor by a

foundation was a gift, not income; Hawley v. Commissioner of Corp. & Tax., 2 A.T.B. 657 (Docket No. 12543, 1939), holding that a federal pension received by the widow of a Civil War veteran was a gift; State Tax Commission v. Gray, 340 Mass. 535 (1960), holding that old-age benefits received under the federal Social Security Act were not retirement allowances taxable under former G.L. c.62 s.5(g); and Bogardus v. United States, 302 U.S. 34, 44 (1937), holding that a gift by a corporation to a former employee was nonetheless a gift for being inspired by gratitude for past service. Whatever the grounds for holding that the payments received in those cases were not compensation for services performed as an employee, the board holds that under the income tax as restructured by St. 1971 c.555 retirement benefits paid by private or public employers, including military pensions, are properly classified as income from employment and thus are includible in Part B gross income under G.L. c.62 s.2(b)(2) unless specifically deductible under other provisions of law. As early as 1920, in

fact, the Legislature provided that any retirement allowance received by a retired employee of the Commonwealth or any local government, or of a corporation, firm, or individual, was to be regarded as "income from profession, employment, trade or business" and taxed as such under St. 1916 c.269 s.5(b), subject to any exemptions therein provided.

The rights of a member of a Massachusetts state or local government retirement system to an annuity, pension, or retirement allowance are exempt from taxation, including income taxes levied under G.L. c.62. G.L. c.32 s.19. Among the items to be deducted in determining Massachusetts gross income pursuant to G.L. c.62 s.2(a)(2), and thus exempted from tax, is the following:

> (E) Income from any contributory annuity, pension, endowment or retirement fund of the United States government or the commonwealth or any political subdivision thereof, to which the employee has contributed.

A deduction from total Part B income is provided for amounts,

not exceeding $2,000, deducted from wages as contributions to those retirement funds. G.L. c.62 s.3(B)(a)(4). See DD 86-12. (As a result of provisions enacted by St. 1987 c.697 ss.75 and 118, such contributions to Massachusetts state or local government retirement funds are treated as employer contributions for federal tax purposes (G.L. c.32 s.22(10)), but remain employee contributions for Massachusetts tax purposes (G.L. c.62 s.2(a)(1)(I). Thus they are not included in Massachusetts gross income; as before, however, amounts received from the retirement fund are included in federal gross income but not in Massachusetts gross income. See LR 87-8.) The result of these provisions for Massachusetts income taxation, taken together, remains that contributions to federal, state, or local retirement systems are not taxed when made, and the retirement benefits themselves are not taxed when received. Income from a contributory fund of another state or a political subdivision thereof which accords a similar exemption for income from Massachusetts funds is

exempt from tax in Massachusetts. G.L. c.62 s.3(B)(a)(4); TIR 89-10.

By the express terms of G.L. c.62 s.2(a)(2)(E), contributory annuities received by civilian employees of the federal government are exempt from Massachusetts taxation. LR 83-38. It is undisputed, however, that the military retirement system is non-contributory and that military personnel make no direct contributions out of their compensation toward the financing of any retirement benefits to which they may be entitled on leaving military service. By the terms of G.L. c.62 s.2(a)(2)(E), therefore, recipients of military retirement benefits from the United States are not entitled to deduct them from federal gross income in determining their Massachusetts gross income.

The appellants contend, however, that taxing their retirement benefits discriminates against them in violation of the constitutional doctrine of intergovernmental immunity as codified in 4 U.S.C. s.111. Decisions of the Supreme Court of

the United States make clear that the doctrine of intergovernmental immunity protects not only the federal government itself and its instrumentalities but also current and retired employees from discriminatory state taxation. Although the Massachusetts statute allows a deduction for all public contributory pensions, federal, state, and local, to which those entitled to them have contributed, and allows no deduction for any non-contributory pension, public or private, the appellants contend (1) that the military retirement system is in effect contributory, because the difference between the levels of military pay and other governmental pay for comparable work amounts to an "imputed contribution," and (2) that there are Massachusetts public employees whose non-contributory pensions are exempt from tax under separate statutes.

The appellants also contend that the discrimination against their retirement benefits violates Article 44 of the Amendments to the Massachusetts Constitution, which authorizes the levy of an income tax.

Intergovernmental Immunity

The doctrine of intergovernmental immunity had its genesis in McCulloch v. Maryland, 4 Wheat. 316 (1819), which held that as applied to the Bank of the United States, a Maryland tax imposed on all banks not chartered by the Maryland legislature unconstitutionally interfered with the functions of an instrumentality of the United States established to carry out the delegated powers of the government of the United States. Later decisions extended the benefit of the doctrine to persons dealing with the United States or its instrumentalities, including federal government employees. For the history of the development of the doctrine in relation to compensation of government employees, see Annotation: "State income tax as violating immunity of United States -- Supreme Court Cases," 103 L.Ed.2d 1027; Paul J. Hartman, Federal Limitations on State and Local Taxation, ss.6.7, 6.15-6.19; as to retirement benefits, see Id., Cum. Supp. January 1992, s.6.24.

The Public Salary Tax Act of 1939 imposed federal income tax on the salaries of state and local government employees and out of considerations of fairness also waived whatever remaining intergovernmental immunity might have shielded federal employees from nondiscriminatory state taxation. As amended, this statute is now codified in 4 U.S.C. s.111, which provides as follows:

> The United States consents to the taxation of pay or compensation for personal service as an officer or employee of the United States . . .by a duly constituted taxing authority having jurisdiction, if the taxation does not discriminate against the officer or employee because of the source of the pay or compensation.

On its face this statute seems to permit the Commonwealth to tax military retirement pay of its residents; but the appellants argue that in taxing military retirement pay, while allowing the deduction of retirement benefits received by state and local employees and federal civil service employees, the Massachusetts income tax discriminates against military employees because of the source of their compensation.

Recent United States Supreme Court Cases

These appeals were brought after promulgation by the Supreme Court of the United States of its decision in Davis V. Michigan Dept. of Revenue, 489 U.S. 803 (1989). A Michigan statute levied an income tax on taxable income, defined as adjusted gross income under the Internal Revenue Code with certain adjustments. Among the adjustments was a deduction in full of retirement benefits received from the state or its political subdivisions and a limited deduction of retirement benefits received from any other retirement system. Davis, a former employee of the federal government, received retirement benefits under the Civil Service Retirement Act and paid taxes on the amount of the benefits received over the limit. In his appeal to the Supreme Court, Davis relied on 4 U.S.C. s.111. In the Court's view, that statute's retention of immunity from discrimination against federal employees because of the source of their compensation was "coextensive with the prohibition against discriminatory taxes embodied in the modern

constitutional doctrine of intergovernmental tax immunity. Cf. Memphis Bank & Trust [Co. v. Garner 459 U.S. 392] at.396-397." 489 U.S. at 813. In an opinion written by Justice Kennedy, the Court decided for the taxpayer; Justice Stevens wrote a dissent.

After the board promulgated its decision in the instant - appeal, the Supreme Court decided the case of Barker v. Kansas, 503 U.S. _ , 118 L.Ed.2d 243, 60 U.S.L.W. 4322 (April 21, 1992), holding expressly that imposing a tax on the retirement benefits of U.S. military personnel, while not taxing retirement benefits of state and local government employees, constituted an invalid discrimination under both the consent provision of 4 U.S.C. s.111 and the constitutional principle of intergovernmental immunity.

Immunity of Current Employees of Government

In Davis v. Michigan, supra, the Court disposed of Michigan's contention that Davis was not entitled to claim

the protection of an imnunity doctrine originally intended to protect the government itself. "It is true that intergovernmental tax immunity is based on the need to protect each sovereign's governmental operations from undue interference by the other. . . . But it does not follow that private entities or individuals who are subjected to discriminatory taxation on account of their dealings with a sovereign cannot themselves receive the protection of the constitutional doctrine. Indeed, all precedent is to the contrary." 489 U.S. at 814 (citations omitted). There is no question that the compensation of current federal employees is protected from discriminatory taxation.

Immunity of Retired Employees of Government

In Davis v. Michigan, supra, the Court also held that the application of 4 U.S.C. s.111 was not limited to the compensation of current employees of the federal government but extended to retirement benefits, which, although deferred, are based and computed on an employee's salary and length of

service, accrue on account of service to the government, and thus "fall squarely within the category of compensation for services rendered 'as an officer or employee of the United States.' " 489 U.S. at 808. As such, the Court held, they are included in the "pay or compensation for personal service as an officer or employee of the United States" against which states are forbidden to discriminate because of its source. 489 U.S. at 809-810.

In Barker v. Kansas, supra, the Kansas court, attempting to distinguish Davis, had held that unlike state retirement benefits, which were deferred compensation for past services, military retirement benefits were "current pay for continued readiness to return to duty." 249 Kan. 186, 196; 815 p.2d 46, 53 (1991). The court based this conclusion on findings that military retirees retired from active duty only but remained members of the armed forces, were still subject to the Uniform Code of Military Justice and could be court-martialed for offenses committed after retirement, were subject to restrictions

on civilian employment after retirement, and were subject to involuntary recall. The military retirement system also differed from the state system in that it was non-contributory, funded entirely by annual congressional appropriations; hence no part of the benefits had ever been taxed. The Kansas court held that the state's taxation of military retirement pay was authorized by 4 U.S.C. s.111, in the same manner as military active-duty pay.

The Supreme Court did not agree that military retirement benefits were pay for current services, pointing out that they were not calculated by reference to continuing duties but based on rank, pay at retirement, and years of creditable service, and that the method of calculation did not differ significantly from that used for determining state retirement benefits. After analyzing other decisions and congressional intent in other provisions relating to military retirement benefits, the Court concluded that for purposes of 4 U.S.C. s.111 military pensions were deferred pay for past services and in this respect were not significantly different from benefits paid to Kansas

state and local government employees.

The board concludes that under 4 U.S.C. s.111 Congress did not consent to discriminatory state taxation of federal retirement benefits.

Explicit Discrimination Favoring State and Local Retirees

In Davis v. Michigan, Michigan argued that its inconsistent treatment of federal and state government retirement benefits was justified by significant differences between them. Of the state's "interest in hiring and retaining qualified civil servants through the inducement of a tax exemption for retirement benefits," the Court said: "This argument is wholly beside the point, however, for it does nothing to demonstrate that there are "significant differences between the two classes" themselves; rather, it merely demonstrates that the State has a rational reason for discriminating between two similar groups of retirees. The State's interest in adopting the discriminatory tax, no matter how

substantial, is simply irrelevant to an inquiry into the nature of the two classes receiving inconsistent treatment." 489 U.S. at 816. Of Michigan's argument that its benefits were "significantly less munificent" than those of the federal government, the Court said: "Even assuming the State's estimate of the relative value of state and federal retirement benefits is generally correct, we do not believe this difference suffices to justify the type of blanket exemption at issue in this case . . . . A tax exemption truly intended to account for differences in retirement benefits would not discriminate on the basis of the source of those benefits, as Michigan's statute does; rather, it would discriminate on the basis of the amount of benefits received by individual employees." 489 U.S. at 817 (citations omitted).

Concluding that the Michigan Income Tax Act violated principles of intergovernmental immunity by favoring state and local government retirees over federal government retirees, the Court ruled that Davis was entitled to a refund of taxes already

paid under the act. On Davis's claim for prospective relief, the Court remanded the case to the Michigan court to resolve questions of state law regarding the appropriate method of complying with the mandate of equal treatment, whether by extending the exemption to retired federal employees or by eliminating the exemptions for retired state and local government employees. 489 U.S. at 818.

In his dissent in Davis v. Michigan, Justice Stevens stated his opinion that the doctrine of intergovernmental immunity did not require a state to give employees of another sovereign more favorable tax treatment than that given to any other group subject to its tax jurisdiction. 489 U.S. at 823. In a concurring opinion in Barker v. Kansas, joined by Justice Thomas, Justice Stevens agreed that the result was controlled by Davis but reiterated his belief that "a state tax burden that is shared equally by federal retirees and the vast majority of the State's citizens does not discriminate against those retirees." 118 L.Ed.2d at 254, 60 U.S.L.W. at 4325. In neither case did

the majority opinion address this question. As the law stands, a tax that favors state and local retirees over federal retirees violates governmental immunity even if the latter are treated no differently than private retirees.

After the publication of the Supreme Court's opinion in Davis, the Commissioner of Revenue stated in a Technical Information Release that the applicable Massachusetts income tax statute does not violate intergovernmental tax immunity doctrine as interpreted in the case (TIR 89-6).

> Unlike Michigan law, the Massachusetts statute does not discriminate on the basis of the source of the benefits. The determining factor for the Massachusetts exemption is whether the retirement fund is a 'contributory fund to which the employee has contributed.' The statutory provisions treat the same way retirement funds of the U.S. government and those of the state and political subdivisions of the state. Therefore, the Davis decision does not affect the Massachusetts tax treatment of federal retirement income, including military retirement income. Any federal retirement income is exempt from Massachusetts tax if the system is contributory and the employee actually contributed.

The board agrees with the Commissioner's analysis.

G.L. c.62 s.2(a)(2)(E) allows a deduction for income from a

contributory retirement fund of the United States government in the same manner as for income from a contributory retirement fund of the Commonwealth or any of its political subdivisions. See TIR 92-3, promulgated after the publication of the decision in Barker v. Kansas. Federal employees who have contributed to their retirement funds are treated more favorably than retirees from private business and more favorably than the taxpayers in Davis v. Michigan or Barker v. Kansas. Federal retirees who have not contributed are treated in the same manner as all other retirees who have not contributed, public or private, with the single exception that will be discussed in the next section.

Government Retirees Favored by Type of Pension

The Massachusetts statute allows the deduction from federal gross income of contributory pensions of employees who have contributed to retirement funds of the United States or of a Massachusetts state or local government. Thus, for income-tax purposes, G.L. c.62 s.2(a)(2)(E) makes two

distinctions: (1) between public and private pensions, and (2) for public pensions, between contributory and non-contributory pensions. In taxing military retirement benefits, the statute does not discriminate in favor of any private pension; it discriminates in favor only of those public pensions which are contributory and whose beneficiaries have contributed to them.

Massachusetts does not allow a general exemption for income from non-contributory state or local retirement funds. Although it appears that some non-contributory local retirement systems exist for veterans who have completed 30 years of state or local government service, the Commissioner of Revenue takes the position that they are includible in Massachusetts gross income when received, except for the return of any contributions made, and that accrued interest paid with such contributions is taxable at the Part A rate. LR 81-53. The appellants argue, however, that exemptions created by the Legislature in 1917 for non-contributory pensions of certain municipal employees discriminate against military retirement

benefits in violation of 4 U.S.C. s.111.

Long before the Legislature restructured the income tax in 1971, it allowed exemptions in 1917 for pensions of Boston public-school teachers (Sp.St. 1917 c.327) and members of local police and fire departments (St. 1917 c.270). If there were enough of the latter surviving in 1973 to justify continuing the exemption (St. 1973 c.876 s.l), there was no evidence than even a few of them are still taking advantage of the exemption. In a series of statutes enacted between 1934 and 1945 the Legislature made all public retirement systems contributory. St. 1934 c.285, St. 1935 c.102, St. 1936 c.318, St. 1945 c.658. The survival of any persons entitled to the exemptions granted in 1917 hardly justifies a finding of current legislative discrimination in favor of local retirees against the beneficiaries of federal non-contributory plans. The appellants made no attempt to prove that any actual discrimination occurred against military retirees as a result of the 1917 exemptions.

The appellants ask the board to ignore the

non-contributory character of the military pension system on the ground that the difference between the scale of military pay and the pay scale of state and local governments amounts in effect to an "imputed contribution" to the military pension system. In the month before the publication of the Supreme Court's opinion in Davis v. Michigan, the Commissioner of Revenue analyzed the question and some of the congressional documents and concluded that the plain meaning of "contributory" required limiting the exemption to contributory plans to which the employees have actually contributed. LR 89-1. The evidence available to the board on this point, like that reviewed by the Commissioner, was at best inconclusive. In Barker v. Kansas, supra, which specifically dealt with discrimination against military pensions, neither the taxpayers nor the Supreme Court made any suggestion that an "imputed contribution" could be inferred from the level of active military pay. The board sees no justification for venturing into territory which the Supreme Court ignored.

The appellants also attack the validity of the distinction between contributory and non-contributory pensions on the ground that contributions of employees account for only about 10 percent of each pension, the remaining 90 percent being appropriated directly from the treasury. If this estimate is accurate, its implications should be dealt with by general legislation and are beyond the power of this board to resolve in the instant appeal.

Article 44 of the Amendments to the Massachusetts Constitution

The Legislature's authority to levy an income tax is contained in a 1915 amendment, Article 44, to the Massachusetts Constitution. The amendment provides in pertinent part as follows:

> Full power and authority are hereby granted to the general court to impose and levy a tax on income in the manner hereinafter provided. Such tax may be at different rates upon income derived from different classes of property, but shall be levied at a uniform rate throughout the commonwealth upon incomes derived from the same class of property. The general court may tax income not derived from property at a lower rate

> than income derived from property, and may grant reasonable exemptions and abatements. . . .

The appellants argue that taxing military retirement benefits, while exempting contributory retirement benefits of state, local, and federal employees, violates the constitutional requirement that the tax on incomes derived from the same class of property be taxed at a uniform rate. The appellants reason that pensions are a single class of property within the meaning of Article 44. They assert that in contributory systems almost 90 percent of the retirement pay is paid by the governmental employer, not by the employee, and argue that as a result the difference between contributory and non-contributory systems is insufficient to justify a difference in tax treatment.

After examining the provisions of G.L. c.32 s.12(2) regarding the composition of the retirement allowances payable under each of the three available options and the provisions of G.L. c.32 s.22 concerning methods of financing of the benefits, the board is not persuaded that the appellants have done justice

to the complexity of the calculations required. Whether by analysis of the statutes or the presentation of evidence, the appellants had the burden of establishing their rights to abatements. A person who claims to be aggrieved by the refusal of the Commissioner to abate a tax in whole or in part has the burden of establishing the right to an abatement. Staples v. Commissioner of Corporations and Taxation, 305 Mass. 20, 26 (1940). See also Commissioner of Corporations and Taxation v. Filoon, 310 Mass. 374, 376 (1941); Stone v. State Tax Commission, 363 Mass. 64, 65-66 (1973).

The appellants cite several cases and opinions involving actual or proposed differentiations that in the Court's opinion violated Article 44: Opinion of the Justices to the Senate and the House of Representatives, 266 Mass. 583 (1929), graduated income tax; Daley v. State Tax Commission, 376 Mass. 861 (1978), different rates on ordinary-income and capital-gain parts, for federal purposes, of a lump-sum payment from an employee pension-plan; Opinion of the Justices to the House of

Representatives, 383 Mass. 940 (1981), an income tax computed as a percentage of the federal tax; Salhanick v. Commissioner of Revenue, 391 Mass. 658 (1984), distinction between mining royalties according to the length of time iron ores were held; and Commissioner of Revenue v. Lonstein, 406 Mass. 92 (1989), taxation of interest from savings deposits according to amount.

In Barnes v. State Tax Commission, 363 Mass. 589 (1973), interest was taxed at the rate of 9 percent with certain exceptions, which included interest made in the course of business by pawn-brokers. G.L. c.62 s.4(a)(1)(ii) as then in effect. The excepted interest was subject to tax at 5 percent under G.L. c.62 s.4(b). The trustees of a trust licensed to make small business loans sought a declaratory judgment that although "loans made in the course of business" was a valid classification, the limitation to pawn-brokers created an unreasonable classification and denied equal protection of the laws. In rejecting the trustees' contention that the limitation was

an attempt to classify persons, not the property to be taxed, the Court said: ". . . . the essential distinction is one of the nature of the business and the incidents which characterize the property employed therein. . . . . It may be added that further limitation of the classification, even if described in terms of persons, which reflects actual underlying differences in the property is allowable under the language of art. 44." 363 Mass. 594.

While holding that taxing interest earned by Massachusetts residents on money deposited in non-Massachusetts financial institutions at a higher rate than interest on money deposited in Massachusetts institutions discriminated against interstate commerce, the Court held that collection and verification difficulties shown by affidavits of revenue officials constituted sufficient "actual underlying differences" between Massachusetts and foreign income to give the Legislature discretion to designate their sources as different classes of property for purposes of Article 44. Aronson v.

Commonwealth, 401 Mass. 244, 254 (1987).

All of these cases deal with the propriety of taxing different classes of income from the same source at different rates, not with the reasonableness of exemptions. Assuming, contrary to Barnes and Aronson, that Article 44 would preclude taxing different classes of pensions at different rates, that is not what G.L. c.62 s.2(a)(2)(E) does. That staute grants an exemption, an act that Article 44 authorizes and that cannot be done without distinguishing one class of income from another. The appellants have not shown, as they must, that the distinction between contributory and non-contributory plans is unreasonable.

The board thinks that in the instant appeal, even if it involved a rate distinction rather than an exemption, the essential distinctions between contributory and non-contributory pensions would be the underlying financial structure of the retirement plan and the prior financial transactions between the plan and its members and that these distinctions are "actual

underlying differences" sufficient to justify the Legislature in designating contributory and non-contributory plans as separate classes for purposes of Article 44.

The board's decision for the appellee was promulgated on October 8, 1991. The board refused the appellants' Consolidated Request for Conclusions of Law, numbers 1 through 6. After the publication of the decision of the United States Supreme Court in Barker v. Kansas, supra, the appellants filed a Motion for Reconsideration on May 4, 1992. After hearing, the board denied the motion.

APPELLATE

TAX BOARD

JOHN E. FILIOS & another[1] *vs.* COMMISSIONER OF REVENUE.

Suffolk. May 3, 1993. - July 13, 1993.

Present: LIACOS, C.J., ABRAMS, NOLAN, & LYNCH, JJ.

Taxation, Income tax. *Constitutional Law*, Income tax. *Retirement*.

Discussion of 4 U.S.C. § 111 (1988), which preserves federal employees' immunity from discriminatory State taxation. [807-809]

Evidence before the Appellate Tax Board did not support a claim that the Commonwealth taxes Federal retirees' military pensions in a discriminatory manner in violation of 4 U.S.C. § 111 (1988), where the Federal military retirement system was a noncontributory system and where the distinction between contributory and noncontributory pension schemes for purposes of State income taxation of distributions is a "significant difference" that warrants different tax treatment of the two classes of taxpayers by allowing exclusion from gross income of benefits received from any contributory retirement system, under G. L. c. 62, § 2 (*a*) (2) (E). [809-812]

Evidence before the Appellate Tax Board did not support a claim that the Commonwealth taxes Federal retirees' military pensions in a discriminatory manner in violation of art. 44 of the Amendments to the Massachusetts Constitution, where the Federal military retirement system was a noncontributory system and where the distinction between contributory and noncontributory retirement systems is an "actual underlying difference" that warrants different tax treatment of the two classes of taxpayers by allowing exclusion from gross income of benefits received from any contributory retirement system, under G. L. c. 62, § 2 (*a*) (2) (E). [812]

APPEAL from a decision of the Appellate Tax Board.

The Supreme Judicial Court granted a request for direct appellate review.

Stephen S. Ostrach for the taxpayers.

[1]Eleanor G. Filios.

Douglas H. Wilkins, Assistant Attorney General (*Thomas A. Barnico*, Assistant Attorney General, with him) for the Commissioner of Revenue.

ABRAMS, J. The plaintiff taxpayers appeal from a decision of the Appellate Tax Board (board) denying them an abatement of the State income tax paid on their military retirement compensation.[2] The taxpayers claim that the taxation is discriminatory, in violation of 4 U.S.C. § 111 (1988), and art. 44 of the Amendments to the Massachusetts Constitution. We granted their application for direct appellate review. We affirm the decision of the board.

1. *Violation of 4 U.S.C. § 111.* The board found that the taxpayers were "residents of the Commonwealth who received income from military retirement compensation from the United States, based on the details of their military service . . . . This compensation was included in the federal gross income of each appellant, and thus became part of each appellant's Massachusetts gross income. Each appellant paid the taxes due on the retirement compensation." The board also found that "[t]he military retirement system is a noncontributory system: military personnel do not have a separate, identified amount deducted periodically from their pay and deposited in a segregated retirement fund from which

[2]The notice of appeal stated that "the Appellants, John E. and Eleanor G. Filios, et al., hereby appeal." The body of the notice of appeal does not indicate to whom the "et al." refers. The commissioner challenged the adequacy of the notice of appeal as to Federal military retirees other than Filios and his wife. In *Cummings* v. *City Council of Gloucester*, 28 Mass. App. Ct. 345 (1990), the Appeals Court has interpreted Mass. R. A. P. 3 (c), as amended, 378 Mass. 927 (1979), consistently with the interpretation given the Federal analogue, Fed. R. A. P. 3 (c), in *Torres* v. *Oakland Scavenger Co.*, 487 U.S. 312 (1988). See also *Rollins Envtl. Servs., Inc.* v. *Superior Court*, 368 Mass. 174, 179-180 (1975) ("[T]he adjudged construction theretofore given to the Federal rules is to be given to our rules, absent compelling reasons to the contrary or significant differences in content"). In *Cummings*, the Appeals Court noted that the United States Supreme Court had ruled that "the term 'et al.' does not satisfy the specificity requirement of Fed. R. A. P. 3 (c), and, unless an appellant is actually named in the notice of appeal, jurisdiction over that party's appeal is lacking." *Cummings* v. *City Council of Gloucester*, *supra* at 347. The only appeal before us is that of John E. and Eleanor G. Filios.

retirement benefits are paid." The board determined that the allowance of an exemption for contributory pension plans did not discriminate against the Federal military retirees.

The taxpayers argue that the Commonwealth treats State and Federal retirement benefits inconsistently and thereby discriminates against them in violation of 4 U.S.C. § 111, which provides: "The United States consents to the taxation of pay or compensation for personal service as an officer or employee of the United States, a territory or possession or political subdivision thereof, the government of the District of Columbia, or an agency or instrumentality of one or more of the foregoing, by a duly constituted taxing authority having jurisdiction, if the taxation does not discriminate against the officer or employee because of the source of the pay or compensation." The United States Supreme Court declared that 4 U.S.C. § 111 is a statute "which preserves federal employees' immunity from discriminatory state taxation." *Davis* v. *Michigan Dep't of the Treasury*, 489 U.S. 803, 807 (1989).

In *Davis*, the United States Supreme Court discussed the congressional purpose in codifying the "nondiscrimination component of the constitutional immunity doctrine which has, from the time of *McCulloch* v. *Maryland*, [17 U.S. (4 Wheat.) 316, 436-437 (1819)], barred taxes that 'operat[e] so as to discriminate against the Government or those with whom it deals.'" *Davis* v. *Michigan Dep't of the Treasury*, *supra* at 812, quoting *United States* v. *Detroit*, 355 U.S. 466, 473 (1958). The Court determined that "the retention of immunity in § 111 is coextensive with the prohibition against discriminatory taxes embodied in the modern constitutional doctrine of intergovernmental tax immunity." *Davis* v. *Michigan Dep't of the Treasury*, *supra* at 813. The Court ruled that the "imposition of a heavier tax burden on [those who deal with one sovereign] than is imposed on [those who deal with the other] must be justified by significant differences between the two classes." *Id.* at 815-816, quoting *Phillips Chem. Co.* v. *Dumas Indep. Sch. Dist.*, 361 U.S. 376, 383 (1960). Therefore, in analyzing whether inconsistent tax

treatment violates § 111, we must determine whether there are "significant differences between the two classes" of taxpayers. See *Barker* v. *Kansas*, 112 S. Ct. 1619, 1622 (1992), quoting *Davis*, *supra* at 816.

Massachusetts defines gross income as "the federal gross income . . . [deducting] [i]ncome from any contributory annuity, pension, endowment or retirement fund of the United States government or the commonwealth or any political subdivision thereof, to which the employee has contributed." G. L. c. 62, § 2 (*a*) (2) (E) (1990 ed.).[3] Thus, the Massachusetts statute exempts from State taxation benefits received through a contributory retirement system. The commissioner states that the pension benefits of the Federal military retirees are taxable, not because the retirees were employed by the Federal government, but because these retirees did not contribute to their pensions.[4] This distinction, the commissioner claims, creates significant differences between the two classes of taxpayers such that differential treatment does not violate 4 U.S.C. § 111.[5] See *Davis* v. *Michigan Dep't of the Treasury*, *supra* at 815. We agree.

[3]General Laws c. 62, § 2 (*a*) (2) (E) (1990 ed.), provides: "Massachusetts gross income shall mean the [F]ederal gross income . . . with the following further modifications: The items to be deducted therefrom are: - Income from any contributory annuity, pension, endowment or retirement fund of the United States government or the commonwealth or any political subdivision thereof, to which the employee has contributed."

[4]In a technical information release (TIR), the commissioner declared that Federal employees who receive benefits from contributory pension plans are exempt from State tax. TIR 92-3 (Apr. 28, 1992).

[5]In *Barker* v. *Kansas*, 112 S. Ct. 1619, 1622-1623 (1992), the State offered six distinctions between military retirees and State and local government pensioners. One of these was that "the federal military retirement system is noncontributory and funded by annual appropriations from Congress," the argument made here. The Court wrote: "As we read the [Kansas Supreme] court, however, it did not rest its decision on this difference . . . . Moreover, we note that the State applies its income tax to other federal retirees who contributed to their benefits, such as members of the Central Intelligence Agency, Foreign Service, bankruptcy judges, and United States magistrates." *Id.* at 1626 n.5. Thus, the Court did not decide whether the fact a retirement system is contributory would be a significant difference sufficient to satisfy the *Davis* v. *Michigan Dep't of the Treasury* test. In any event, the Kansas State tax system apparently did

The term "contributory" is not defined in the statute. In a technical information release (TIR), the commissioner defined a contributory retirement plan as one "in which amounts contributed to the plan are includible in the Massachusetts gross income of the employee (or would be included in the Massachusetts gross income of the employee if the employee were a Massachusetts resident). Under a noncontributory plan, amounts contributed on behalf of an employee are not included in the gross income of the employee and are therefore not subject to tax at the time of contribution. Thus, taxing distributions from contributory plans can lead to double taxation, while taxing distributions from noncontributory plans will not." TIR 92-3 (Apr. 28, 1992). See Black's Law Dictionary 329 (6th ed. 1990) (A "contributory" pension plan is one "where employees, as well as employers, make payments to a pension fund").

Under G. L. c. 62, § 2 (*a*) (2) (E), the tax treatment of retirement benefits depends on the pension plan. As TIR 92-3 states, employees already have been taxed on the contributions they make to their pensions. Federal employees who contribute to their pensions are not taxed on the benefits received. See note 4, *supra*. There is no violation of 4 U.S.C. § 111.

The taxpayers argue that the distinction between contibutory and noncontributory pensions systems is illusory. They assert that 90% of the State retirement benefits are noncontributory because they come from contributions made by the employees' governmental units. See G. L. c. 32, § 1 (1990 ed.). Therefore, they argue, the complete exemption from taxation of all of the retirement benefits of State and local employees undercuts the commissioner's reliance on that distinction.

not use the distinction between contributory and noncontributory retirement systems in determining whether certain pension benefits would be subject to taxation. See *Barker* v. *Kansas*, *supra* at 1621 n.1.

The Legislature has chosen to exempt pensions to which an employee contributes and has not defined a contributory plan to include a minimum percentage contribution by the employee. See G. L. c. 62, § 2 (*a*) (2) (E). The fact that the State employee contributes only 10% is not sufficient to negate the differential tax treatment between the pension systems.

The taxpayers also note that the noncontributory pensions of certain State and municipal retirees are exempt from State income tax. When the Commonwealth first enacted the State income tax, it exempted the noncontributory pensions of Boston school teachers and all municipal police and fire personnel. See Spec. St. 1917, c. 327; St. 1917, c. 270. Then, in 1973, the Legislature again provided that the pensions received by employees of municipal fire and police departments who were employed before the establishment of the contributory retirement system and who did not choose to join the contributory retirement system, would be exempt. St. 1973, c. 876, § 1. The taxpayers claim that this exemption creates a violation of 4 U.S.C. § 111.

The board found that the "exemptions were enacted in 1917, the year after the imposition of the income tax. In order to be covered by a noncontributory plan whose exemption was confirmed by St. 1973, c. 876, § 1, an employee in the police or fire service of a city or town would have to have been in active service when the contributory system under Chapter 32 was established in 1936 or 1937 and elected not to join it. If any qualifying employees existed during the tax years at issue, it was the responsibility of the appellants to produce evidence of the fact. Because no such evidence was furnished to the board, no finding could be made by the board that the class established by St. 1917, c. 270, and confirmed by St. 1973, c. 876, had any members during the years at issue. Further, the board notes that the active life of a person in the police or fire service would be unlikely to have continued for fifty-five years from 1936, when the municipal retirement plans were made contributory, to 1991. If the class had any members during the years at issue, it is

unlikely that they were numerous, or that they will survive long enough to require legislative action to remove their more favorable treatment or give similar treatment to military retirees." We conclude that the distinction between contributory and noncontributory pensions systems was a valid one for the Legislature to make and for the board to follow.

The Commonwealth does not impose the tax based on the source of the income, see note 3, *supra*; it looks rather to whether the employee contributed to the plan. Contrary to the plaintiffs' argument, that distinction is not illusory. *Davis* does not require a different result. The evidence before the board does not support a claim that the Commonwealth is taxing Federal retirees in a discriminatory manner.

2. *Violation of art. 44.* Article 44 states in part: "Full power and authority are hereby given and granted to the general court to impose and levy a tax on income in the manner hereinafter provided. Such tax may be at different rates upon income derived from different classes of property, but shall be levied at a uniform rate throughout the commonwealth upon incomes derived from the same class of property." The taxpayers claim that taxing the retirement benefits of State and municipal retirees at a "0% rate" and taxing them at a different rate violates art. 44. We disagree.

"Properties are of the same kind unless there are 'actual underlying differences between them.'" *Commissioner of Revenue* v. *Lonstein*, 406 Mass. 92, 94 (1989), quoting *Salhanick* v. *Commissioner of Revenue*, 391 Mass. 658, 662 (1984). The commissioner satisfied the test for significant differences under *Davis* v. *Michigan Dep't of the Treasury*, *supra*. We hold that the distinction between a contributory retirement system and a noncontributory retirement system is an actual underlying distinction, sufficient to meet the test of *Lonstein*.

The construction advocated by the plaintiffs would favor Federal retirees over State retirees. The legislative distinction between contributory and noncontributory pensions is fair to

all retirees. The decision of the Appellate Tax Board is affirmed.[6]

So ordered.

[6]On Friday, June 18, 1993, the United States Supreme Court issued its opinion in *Harper* v. *Virginia Dep't of Taxation*, 61 U.S.L.W. 4664 (June 15, 1993). That case is inapplicable because its sole issue was that of the retroactivity of the rule announced in *Davis* v. *Michigan Dep't of the Treasury*, *supra*.

COMMONWEALTH OF MASSACHUSETTS

SUPREME JUDICIAL COURT FOR THE COMMONWEALTH

In the case No. SJC-06066

JOHN E. FILIOS & others[1]

vs.

COMMISIONER OF REVENUE

O R D E R

The request to reconsider the plaintiffs' motion to amend the notice of appeal to separately name the 27 individuals consolidated in the trial court is hereby allowed for purposes of seeking review in the Supreme Court of the United States. The docket shall reflect the allowance of the motions. The published opinion of this court will remain unchanged.

By the Court (Abrams, J.).

ENTERED: October 26, 1993

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[1] Eleanor G. Filios, Herbert L. Cheeseman, Betsy B. Cheeseman, Ralph Cipolla, Doris H. Cipolla, Joseph M. Conroy, Robert C. Davenport, Annetta B. Davenport, Kenneth R. Depperman, Mary E. Depperman, Charles F. DeSmet, Marjorie I. DeSmet, Francis H. Fumia, Dreama F. Fumia, Mack K. Greenberg, Harriet C. Greenberg, Daniel F. Hayes, Dorothy R. Hayes, David J. Mainville, Vern Mainville, Donald G. Smith, Ruth E. Smith, Richard J. Spatafora, Liliane M.J. Spatafora, Russell E. Tracy, Lillian A. Tracy.